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CITATIONS

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Cases—Continued

Miscellaneous:

In the Supreme Court of the United States

OCTOBER TERM, 1972

No. 72–654

UNITED STATES OF AMERICA, PETITIONER

v.

ARCHIE L. MASON, ET AL.

ON WRIT OF CERTIORARI TO THE UNITED STATES COURT OF CLAIMS

BRIEF FOR THE UNITED STATES

OPINION BELOW

The opinion of the Court of Claims (Pet. App. A) [1] is reported at 461 F. 2d 1364.

JURISDICTION

The judgment of the Court of Claims was entered on June 16, 1972. Pursuant to orders extending the time within which to file a petition for a writ of certiorari, petitions were filed by the State of Oklahoma (No. 72–606) and the United States (No. 72–654) on October 16, 1972, and October 27, 1972,

[1] For convenience we shall refer to the appendix in No. 72–606 as "Pet. App."

respectively. Both petitions for certiorari were granted on January 15, 1973, and the cases were consolidated. This Court's jurisdiction rests on 28 U.S.C. 1255(1).[2]

QUESTIONS PRESENTED

1. Whether the United States as trustee is liable to the estate of a restricted Osage Indian for breach of fiduciary duty because it paid State inheritance taxes to the State of Oklahoma in 1967 and 1968 from funds of the estate, as required by this Court's decision in *West* v. *Oklahoma Tax Commission,* 334 U.S. 717, instead of attempting to have *West* overruled.

2. Whether *West* v. *Oklahoma Tax Commission* should be overruled.

STATEMENT

Under the Osage Allotment Act of 1906, 34 Stat. 539, Osage tribal lands were alloted to the enrolled tribal members but subject to restrictions on alienation until the owners receive certificates of competency. The Act provides for a delayed allotment of the Tribe's mineral interest. Until the trust period expires in 1984, the interests are to be held by the Tribe subject to federal supervision but during that time the revenues from the mineral interests are to be held in trust by the United States for the members of the Tribe with periodic distribution of royalties to the

[2] 28 U.S.C. 1255 does not on its face provide for a third-party defendant in the Court of Claims, like the State of Oklahoma, to petition for certiorari. However, 41 U.S.C. 114 (b) states that such third-party defendants shall be treated for all purposes as claimants, and 28 U.S.C. 1255(1) specifically allows claimants to petition for certiorari.

members. 34 Stat. 543–544. Other tribal funds, including the proceeds of sales of tribal lands in Kansas, are also to be held in trust by the United States. 34 Stat. 544. The Act provides that the lands, moneys and mineral interests of any deceased Osage shall, with certain exceptions, descend to his legal heirs according to the law of what is now the State of Oklahoma. 34 Stat. 545. At the termination of the trust, as now extended to 1984 (52 Stat. 1034, Sec. 3), "the lands, mineral interests, and moneys * * * held in trust by the United States shall be the absolute property of the individual members of the Osage tribe * * * or their heirs." 34 Stat. 544. The present right of a tribal member in this trust fund is commonly referred to as his "headright."

Amendments to the Osage Allotment Act in 1912 and in 1947 (37 Stat. 86, 88; 61 Stat. 747) specify that the land and funds held in trust or under restriction "shall not be subject to lien, levy, attachment, or forced sale * * * prior to the issuance of a certificate of competency." 61 Stat. 747.

In 1948, this Court held in *West* v. *Oklahoma Tax Commission,* 334 U.S. 717, that the State of Oklahoma could lawfully levy inheritance taxes on the transfer of the estates of retricted Osage Indians, including the portions of such estates held in trust by the United States, upon the death of the beneficial owner. The trust properties in *West,* as in the present case, consisted of headrights in Osage mineral interests, and other tribal funds and re-investments of funds.[3]

[3] Compare Pet. App. A–4 with 334 U.S. at 719.

In 1967 and 1968, after the death of Rose Mason, a non-competent Osage Indian domiciled in Oklahoma, the Osage Agency of the Bureau of Indian Affairs, Department of the Interior, acting in accordance with this Court's decision in *West*, paid to the Oklahoma Tax Commission $8,087.10 in inheritance taxes on the passage of her estate to her heirs at law (Pet. App. A–4). These payments were made out of trust funds of the decedent held by the government as trustee. In November 1970 the administrators of her estate brought the present suit against the United States in the Court of Claims, alleging that the decision in *West* had been so weakened by subsequent cases that the United States, as a fiduciary, was obliged to challenge the tax, and not to pay it (Pet. App. A–5). To support their contentions, the administrators of the Mason estate chiefly relied on this Court's decision in *Squire* v. *Capoeman*, 351 U.S. 1, and subsequent decisions by courts of appeals and revenue rulings by the Treasury Department.

The Court of Claims, acknowledging that *West* "is the last word from the Supreme Court directly on point" (Pet. App. A–9), nevertheless agreed with the administrators and held that: "the *West* result is no longer controlling * * *" (Pet. App. A–24), that the government's payment of the tax without challenge was a breach of its fiduciary duty to the Mason estate, that the measure of damages is the full amount of tax paid, and that the United States is liable in that amount to the estate. It further held that the United

States is entitled to be indemnified by the State of Oklahoma in the same amount.

SUMMARY OF ARGUMENT

I. The United States did not violate its duty to the estate of Rose Mason by paying the Oklahoma inheritance tax assessed against her estate. While a trustee has a duty to preserve the trust estate, part of this duty is to pay taxes as they come due. This Court had previously held in *West* v. *Oklahoma Tax Commission,* 334 U.S. 717, that the identical trust is not exempt from Oklahoma inheritance taxes. A subsequent decision, *Squire* v. *Capoeman,* 351 U.S. 1, held that the General Allotment Act, 24 Stat. 388, 25 U.S.C. 331 *et seq.,* provides a certain immunity from federal income taxation but did not overrule or question *West.* In 1967 and 1968, when the United States paid these taxes, a number of the decisions and executive actions relied upon by respondent had not yet occurred. The decision to pay the tax was, consequently, a proper exercise of discretion by the trustee.

II. There has long been a distinction between taxes on property and taxes on the transfer of property, particularly the transfer which occurs at death. On this basis the decision in *West* is distinguishable from *Squire.*

It is clear, however, that the approach taken by the Court in *Squire* was different from that of *West* and that this difference has had its effect on lower court decisions and executive actions. Whether *West*

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has in fact been impaired, and, if so, whether that impairment is fatal to its continued vitality, can only be determined by this Court. The question of the right of Oklahoma to tax estates such as this will arise regularly during the course of the trust. It is important, therefore, that the law be clarified.

ARGUMENT

I. THE UNITED STATES DID NOT VIOLATE ITS DUTY AS TRUSTEE IN PAYING THE OKLAHOMA INHERITANCE TAX ASSESSED ON THE ESTATE OF ROSE MASON IN ACCORDANCE WITH THIS COURT'S DECISION IN WEST V. OKLAHOMA TAX COMMISSION

1. The Court of Claims has held that the United States is surchargeable for the entire amount of the estate taxes paid by the government in its capacity as trustee in conformity with an outstanding decision of this Court squarely holding the trust liable for the taxes. Not only did the Court of Claims forecast that this Court will overrule the otherwise controlling decision but it also concluded that the government's conduct in failing to seek the overruling constituted a breach of the fiduciary duty to exercise good faith and reasonable competence. This ruling by the court below lacks support in general trust law or in either the historic or the current relationship between the federal government and Indian trusts.

Whether *West* v. *Oklahoma Tax Commission,* 334 U.S. 717, is ultimately reaffirmed or overruled by this Court, the decision of the Court of Claims holding the government liable for breach of fiduciary

duty should be reversed. The relevant general principle has been stated as follows: "A trustee is under a duty in administering the trust to exercise such care and skill as a man of ordinary prudence would exercise in dealing with his own property."[4] The United States has not violated this duty of care. It is, of course, correct that the government had a fiduciary duty to preserve the estate of Rose Mason—not to pay a tax that is clearly not owed. But as with any prudent trustee, the government as trustee also has the duty to pay taxes as they come due:

> Similarly the trustee is under a duty to protect the trust property by paying taxes thereon. If he has funds available for the purpose and fails to pay the taxes with the result that the land is sold, the trustee is subject to a surcharge. So also if owing to the negligence of the trustee in delaying the payment of taxes penalties are incurred, the trustee is subject to a surcharge for the amount of the penalties.[5]

The decision whether to pay a tax, or to contest it, thereby risking penalties and litigation costs and expenses, is thus not a simple one. The competing considerations require that the trustee have a "certain amount of discretion"; in accordance with the traditional standard of fiduciary responsibility, the trustee will be held liable to a surcharge "only if he abuses the discretion by failing to do what is reasonable un-

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[4] 2 Scott, *The Law of Trusts* (3d ed.), § 174, p. 1408. See also Bogert, *Trusts and Trustees* (2d ed.), § 582, p. 216. These treatises are hereinafter cited as "Scott" and "Bogert" respectively.

[5] 2 Scott, § 176, p. 1422. See also Bogert, § 602, p. 383.

der the circumstances."[6] Professor Scott explains, with particular relevance to the present case:

> * * * He [the trustee] does not necessarily act unreasonably in paying a claim, even though he believes that the claim is not well founded, if under all the circumstances, in view of the amount involved and the doubt as to the issue, it appears to be not unreasonable to pay the claim. Thus it has been held that where the question of the liability of the trust estate for an inheritance tax in another state for a small amount was debatable and it would cost more than the amount of the tax to litigate the question, the trustee was not subject to a surcharge for paying the tax, even though in fact the estate was not subject to the tax.[7]

2. In order to consider whether the government has failed to meet its fiduciary responsibility by paying Oklahoma estate taxes out of Rose Mason's share of the Osage trust, it is therefore essential to consider the circumstances at the time the government acted to pay these taxes in 1967 and 1968.

In *West,* decided in 1948, this Court held that Oklahoma can assess its inheritance tax on the transfer at death of Osage headrights. The fund and the tax were the same as those now before the Court. Relying on its earlier decision in *Oklahoma Tax Commission* v. *United States,* 319 U.S. 598, the Court found that Congress had not provided an express immunity from taxation

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[6] 2 Scott, § 178, p. 1428.

[7] 2 Scott, § 178, pp. 1428–1429, citing *Selleck* v. *Hawley,* 331 Mo. 1038, 1056, 56 S.W. 2d 387, 395–396; *Patterson* v. *Vivian,* 137 App. Div. 596, 122 N. Y. Supp. 347. See, also, Gross, *Liability of Trustees for Inheritance Taxes of Foreign States,* 96 Trusts & Estates 444 (1957).

in the Osage Allotment Act (334 U.S. at 727–728) and that it could not imply such an immunity. The Court also distinguished between a tax on the trust fund itself and a tax on the transfer of the property to another (334 U.S. at 727), though it was aware that the economic effect of either tax could be the depletion of the trust corpus (*id.* at 725–726).[8]

Seven years later, without any reference to *West*, the Court decided *Squire* v. *Capoeman*, 351 U.S. 1, which the court below concluded "seriously weakened or eroded" the decision in *West* (Pet. App. A–18). In *Squire* this Court held that, despite the absence of an express tax exemption, the government's statutory duty under the General Allotment Act of 1887, 24 Stat. 388 (25 U.S.C. 331 *et seq.*) to return lands to Indian allottees free of any lien or encumbrance[9] prohibited the United States from assessing a capital gains tax on the profit resulting from the government's sale of timber produced on the allotted trust land. The Court stated that "to protect the Indians' interest * * * it is necessary to preserve the trust and income derived directly therefrom, but it is not necessary to exempt reinvestment income from tax burdens." 351 U.S. at 9. The Court also relied on language in an amendment to the General Allotment

[8] In *Oklahoma Tax Commission* v. *United States*, the government had argued that the State of Oklahoma is without power to impose a tax upon the transfer of restricted property of members of the Five Civilized Tribes, including restricted funds managed by the United States. The Court ruled against the government. In *West*, the Court found no practical difference between restricted funds and funds held in trust.

[9] The Osage Allotment Act contains similar, though not identical, language, see p. 3 *supra*.

Act providing for taxation of the land after the allottee receives a patent in fee. 351 U.S. at 7.[10]

While *Squire* contains broad and important language concerning implied tax immunities on restricted or trust property (see, *e.g.*, 351 U.S. at 6–7), it is essentially a decision concerning federal income taxation on income derived from allotted lands, preventing the government from collecting a tax on the gain resulting from a sale of timber from such land.

We doubt that anyone in 1955 thought that *Squire* was so inconsistent with *West* that it could be taken as tacitly overruling that case. Indeed, in *Kirkwood* v. *Arenas*, 243 F. 2d 863, decided shortly after *Squire*, and also relied on by the court below (Pet. App. A–10, A–12), the Ninth Circuit held California inheritance taxes inapplicable to trust allotments of Agua Caliente Indians but carefully distinguished *West* as based on an allotment act not conferring the tax exemption that was provided by the General Allotment Act as made applicable to the lands of the Agua Caliente Indians in that case by the Mission Indian Allotment Act.

We recognize that *Squire* v. *Capoeman* has been extended by lower courts to other related contexts. Thus, while that decision involved the federal capital gains tax on a sale of timber, the Court of Claims in 1962 held that under *Squire* income from Osage headrights is exempt from federal income taxation. See

[10] The Osage Allotment Act does not contain such language as to headrights but does as to allotments of land. 34 Stat. 542. See *West* v. *Oklahoma*, *supra*, 334 U.S. at 724–725.

Big Eagle v. *United States*, 300 F. 2d 765. See, also, *United States* v. *Hallam*, 304 F. 2d 620 (C.A. 10).

The United States has also interpreted *Squire* generously but not as generously as the Court of Claims. In 1959, the Treasury Department ruled on the basis of *Squire* that income derived by an Indian directly from trust land held under the General Allotment Act or similar acts would not be subject to federal income taxation. Rev. Rul. 59–349, 1959–2 Cum. Bull. 16. This ruling was repeated and refined in 1967 in Rev. Rul. 67–284, 1967–2 Cum. Bull. 55. In the meantime, it had been held in *Nash* v. *Wiseman*, 227 F. Supp. 552 (W. D. Okla.), in 1963 that under *Squire* allotted land and trust fund cash held by the government for a restricted Indian are not subject to federal estate taxation. In 1967 the issue as to federal estate tax was again in litigation in the Western District of Oklahoma and in January 1968 was decided adversely to the government in *Asenap* v. *United States*, 283 F. Supp. 566. It was during this period, 1967–1968, that the United States paid the Oklahoma inheritance tax on the Mason estate. Not until 1969, after the government paid the state inheritance taxes at issue in the present case, did the Internal Revenue Service conclude that the rationale of *Squire* should apply to federal estate taxes as well as to income taxes. Rev. Rul. 69–164, 1969–1 Cum. Bull. 220.

3. To recapitulate, at the time the government, acting as trustee, paid $8,087 in Oklahoma inheritance taxes in 1967 and 1968, this Court's decision in *West* v. *Oklahoma Tax Commission* holding Oklahoma inheritance taxes applicable to the transfer of Osage headrights was unquestioned by any later decision of this

Court. A subsequent case, *Squire* v. *Capoeman*, had recognized an immunity from *federal income* taxation as being implicitly created by the General Allotment Act. The Treasury Department and the lower courts were defining the extent of the exemption as applied to different kinds of income and different allotment acts. The question whether *Squire* had any effect on the right of the federal government to collect estate taxes on allotted lands and shares in trust funds was being litigated. And not until after these taxes were paid did the government conclude that federal estate taxes were not applicable to such property. The one case (*Kirkwood* v. *Arenas, supra*) holding that state inheritance taxes could not be assessed against restricted lands had carefully distinguished *West*, implicitly conceding its vitality on its facts.

Moreover, though individual Indians are free to contest payments of taxes out of trust funds and there is a vigorous bar ready to handle such cases (*West* itself was such a case, as is the present one), no individual suit had been brought contesting the obligation of the United States to obey the *West* decision in administering Osage trust funds.

Under these circumstances, we submit, it would have been at least a serious question whether a prudent trustee could properly have refused to pay the tax. A refusal to pay, if not ultimately sustained, would have exposed the trust to penalties and other clouds. Seeking a judicial test of *West* would necessarily have had to be pressed for ultimate consideration by this Court, and would have meant long and costly litigation. Unless the government is to be held to something akin to

an insurer's absolute liability rather than to the standard of good faith competence applicable to trustees in general, we submit that there was no warrant for finding that a fiduciary duty was violated in not challenging this Court's decision in *West*. Under all the circumstances, the course taken by the government was within the range of reasonable options open to a prudent trustee, and the surcharge for the amount of the taxes paid was improper.[11]

II. THE QUESTION OF THE CONTINUED VALIDITY OF THE OKLAHOMA INHERITANCE TAX ON THE TRANSFER OF OSAGE TRUST PROPERTY SHOULD BE DECIDED BY THIS COURT

On the underlying question in this case, the Department of Justice is in a difficult position. On the one hand, it represents the Department of the Interior, which has a fiduciary responsibility to the Osage Indians, and particularly to the respondents here, who are administrators of the estate of a deceased Osage Indian. On the other hand, the Department has a professional, and thus a fiduciary, responsibility to the United States, and, in an appreciable sense, to the law. An overruling of this Court's decision in *West* v. *Oklahoma Tax Commission*, 334 U.S. 717, might well have an adverse impact on the

[11] To the extent the Court affirms all or part of the surcharge imposed by the Court of Claims, the government stands by that part of the decision below (Pet. App. A–25) that grants judgment to the government on its third-party complaint against the State of Oklahoma, also a petitioner before this Court, for reimbursement of any taxes held to have been erroneously paid.

revenue interests of the United States under such cases as *Helvering* v. *Mountain Producers Corp.*, 303 U.S. 376, which was one of the authorities on which this Court relied in reaching its *West* decision. As this Court said, speaking through Mr. Justice Black, in *Oklahoma Tax Commission* v. *United States*, 319 U.S. 598, 610:

> Recognizing that equality of privilege and equality of obligation should be inseparable associates, we have recently swept away many of the means of tax favoritism. *Graves* v. *New York ex rel. O'Keefe*, 306 U.S. 466, permitted states to impose income taxes upon government employees, and *Helvering* v. *Gerhardt*, 304 U.S. 405, permitted the federal government to impose taxes on state employees. *O'Malley* v. *Woodrough*, 307 U.S. 277, overruled a previous decision which held that judges should not pay taxes just as other citizens, and *Helvering* v. *Mountain Producers Corp., supra*, repudiated former decisions seriously limiting state and federal power to tax. See also *Metcalf & Eddy* v. *Mitchell*, 269 U.S. 514, and *James* v. *Dravo Contracting Co.*, 302 U.S. 134. The trend of these cases should not now be reversed.

Thus there is a clear conflict of interest. If there were a way to avoid it, it should be followed. The President has recommended the establishment of an Indian Trust Counsel Authority, with broad powers to represent the interests of Indians, in all courts, state and federal. See "The American Indians—Message from the President of the United States," 116 Cong. Rec. 23,131 (1970). But no such authority has been established.

In this situation, the only resolution seems to be for the Department to try to present the questions as fairly as possible, without advocacy one way or the other, in the hope that it may be of some assistance to the Court in coming to a conclusion.

There has long been a distinction in our law between taxes on property, and taxes on the transfer of property, particularly the transfer which occurs at death. Thus, in *Plummer* v. *Coler,* 178 U.S. 115, the Court sustained a state inheritance tax as applied to the value of federal bonds, although Congress had by the Act of July 14, 1870, under which the bonds were issued, declared "that the principal and interest were exempt from taxation in any form by or under state, municipal or local authority" (178 U.S. at 118), and this was only a few years after a similar constitutional immunity had been declared in *Pollack* v. *Farmers Loan and Trust Co.,* 157 U.S. 429, 584. See also *Murdock* v. *Ward,* 178 U.S. 139, holding that similar bonds, with a similar statutory tax exemption, could be subjected to a federal inheritance tax. In *Greiner* v. *Lewellyn,* 258 U.S. 384, the Court held that the federal estate tax could be applied to bonds issued by state municipalities. In *United States Trust Co.* v. *Helvering,* 307 U.S. 57, the Court held that proceeds of war risk insurance were subject to the federal estate tax despite a provision in the statute that such "insurance . . . shall be exempt from all taxation."

In 1943, in *Oklahoma Tax Commission* v. *United States, supra,* the United States argued, in a detailed brief, that Oklahoma inheritance taxes could not be

applied to restricted Indian lands and funds.[12] The United States argued that "in the absence of congressional authority no state can use these lands as the subject or the measure of a tax" and that as to the Oklahoma inheritance tax "(1) the tax itself, (2) the lien of the tax, and (3) certain of its administrative features, are each contrary to the Federal restriction" (Br. p. 71). The Court, however, decided to the contrary, allowing the application of the state inheritance tax to restricted lands and funds as to which there was no express tax exemption.

Thereafter, in *West,* the Court refused to distinguish for tax purposes between restricted funds, which were at issue in *Oklahoma Tax Commission,* and trust funds, which are at issue here and in *West.* The Court recognized in *West* that "[i]f the estate is to be tapped repeatedly by Oklahoma until 1984 by the deaths of the various heirs, the result may be a substantial decrease in the amount then available for distribution." 334 U.S. at 726. Nevertheless, the Court declined to hold the Oklahoma tax inapplicable to these funds.

Twenty-five years have passed since *West* was decided. Although Congress rarely acts on such matters, its inaction here may possibly be of some significance.

Although the decision in *West* seemed definitive, there have been currents in the other direction since *West* was decided. In 1956, the Court decided *Squire* v. *Capoeman,* 351 U.S. 1, in an opinion by Chief Justice Warren. That case involved the federal income

[12] See Brief of the United States, Nos. 623–625, October Term, 1942.

tax as applied to a capital gain resulting from the sale by the government of standing timber on allotted forest land on an Indian reservation, held in trust for an Indian. In denying the tax, the Court held that an amendment to the General Allotment Act created a tax exemption by implication, in that it required the return of the trust property without encumbrances at the end of the trust period, and provided for taxation after the termination of the trust. Moreover, the general purport of the decision is one of liberality in finding tax immunity where Indian property is concerned.

Thereafter, the Court of Claims in *Big Eagle* v. *United States,* 300 F. 2d 765, held that the Osage Allotment Act—at issue here—is, for tax purposes, essentially indistinguishable from the General Allotment Act, and provides the same immunity against federal income taxation that this Court found in *Squire* v. *Capoeman.* The United States, in the compromise of *Beartrack* v. *United States,* No. 281–67, in the Court of Claims and in Rev. Rul. 69–164, 1969–1 Cum. Bull. 220, has accepted this position and no longer seeks to assess its income taxes against revenues produced by Osage headrights or to assess an estate tax against these headrights, except for earnings on reinvestment.

No decision of this Court has referred disparagingly to *West* v. *Oklahoma Tax Commission, supra.* And it is clear that the *West* decision, as a precedent, is distinguishable from that reached in *Squire* v. *Capoeman, supra,* since *West* involved a state inheritance tax on the transfer of property held in trust for Osage

Indians, while *Squire* involved a federal income tax on the gain from the sale of allotted property held in trust for a Quinaielt Indian, involving different statutory provisions.

It is equally clear, though, that the approach taken in *Squire* was different from that which had been followed in *West* less than eight years previously. This difference in approach has had its impact both on lower courts and, as a result of these lower court decisions, on the Executive branch of the government. Whether *West* has in fact been impaired, and, if so, whether that impairment is fatal to its continued vitality can only be determined by this Court. In this connection, it may be observed that *Squire* v. *Capoeman* expressly declined to establish a tax exemption for reinvested property; thus if *Squire* is held to vitiate *West*, the question still remains how much of the Mason estate may now enjoy an exemption from Oklahoma inheritance taxes.

The Osage trust, unless modified by Congress, will remain in effect until 1984. During that time the question of the right of Oklahoma to tax estates such as this will arise regularly. It is important, therefore, that the law be clarified so that the United States, as trustee, may know whether it remains bound to pay such taxes, and if so, on what portions of the decedents' estates.

CONCLUSION

For the foregoing reasons, the judgment of the Court of Claims against the United States should be reversed.

Respectfully submitted.

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